UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF NEW YORK

FEDERAL INSURANCE COMPANY, Plaintiffs, v. THE ESTATE OF IRVING GOULD, MEHDI ALI, ALEXANDER M. HAIG, JR., THE ESTATE OF RALPH SELIGMAN, BURTON WINBERG and J. EDWARD GOFF, Defendants.	No. 10 Civ. 1160 (RJS)
THE ESTATE OF IRVING GOULD, MEHDI ALI, ALEXANDER M. HAIG, JR., THE ESTATE OF RALPH SELIGMAN, BURTON WINBERG and J. EDWARD GOFF, Third-Party Plaintiffs, v. CHARTIS INSURANCE COMPANY OF CANADA (f/k/a American Home Assurance Company (Canada Branch)) and TRAVELERS CASUALTY AND SURETY COMPANY (f/k/a The Aetna Casualty and Surety Company), Third-Party Defendants.	

THIRD PARTY DEFENDANT TRAVELERS CASUALTY AND SURETY COMPANY'S (f/k/a THE AETNA CASUALTY AND SURETY COMPANY) MEMORANDUM OF LAW IN OPPOSITION TO DEFENDANTS' MOTION FOR PARTIAL SUMMARY JUDGMENT

Travelers Casualty and Surety Company (f/k/a the Aetna Casualty and Surety Company) ("Travelers") submits this memorandum of law in opposition to Defendants' Motion for Partial

Summary Judgment on the Insurance Companies' Exhaustion Defenses. Pursuant to the Court's direction to limit redundant briefing, Travelers hereby joins in, and incorporates by reference, as if fully set forth herein, unless otherwise specified, (i) Federal Insurance Company's Opposition to Defendants' Motion for Partial Summary Judgment (the "Federal Opposition"); and (ii) Federal Insurance Company's Response to Defendants' Statement of Undisputed Facts ("Federal's Local Rule 56.1 Statement") including the reservation of right to object to any facts asserted in Defendants' Statement of Undisputed Facts [ECF No. 48].[1]

PRELIMINARY STATEMENT

As explained in the insurers' motions for judgment pursuant to Rule 12(c) [ECF Nos. 38-43] and the Federal Opposition, the Travelers Policy, provides coverage for "loss" as defined in the policy. It has a Limit of Liability of $10 million in excess of $40 million in required underlying insurance. The plain and unambiguous language of the Travelers Policy provides that coverage is triggered upon exhaustion of Underlying Insurance "solely as the result of actual payment of losses." The undisputed facts, however, establish that the underlying policies have not been and are not likely to be exhausted. The undisputed evidence is that two of the underlying carriers (Reliance and The Home) are insolvent and have not made any payment whatsoever.

Despite the clear language of the Travelers Policy requiring exhaustion by payment, controlling Pennsylvania law, and the undisputed fact that The Home and Reliance policies are not and will not be exhausted, the Commodore D&Os now seek partial summary judgment. They seek a declaratory judgment that the Travelers Policy is triggered once Defendants' defense

[1] Unless otherwise noted, capitalized terms have the same meaning as set forth in Travelers' Motion for Judgment on the Pleadings ("Travelers' Rule 12(c) Motion"). [ECF Nos. 41-43]

costs and/or liability reaches $40 million**,** even though, owing to the Reliance and The Home insolvency, ***no one actually pays*** much of the initial $40 million in loss**.**

In other words, they effectively argue that the exhaustion requirement of the Travelers Policy is meaningless. If the Court were to grant such relief, under the D&Os' theory, the D&Os could enter into a $50 million settlement of the Bahamian Litigation, which they would have this Court hold requires Travelers to pay its $10 million limits notwithstanding that (assuming full exhaustion of the $21 million in Federal and Chartis coverage), $19 million of the first $40 million in loss created by the putative settlement is never paid by anyone.

As explained in the Federal Opposition, and below, exhaustion of the underlying coverage is a condition precedent to Travelers coverage obligations. However, if the D&Os are correct and non-exhaustion by The Home and Reliance does not relieve Travelers of coverage obligations, at the very least, the policy language, law and facts mandate that Travelers cannot be obligated to pay any loss until $40 million of loss has, ***in fact, been paid,*** whether by the underlying carriers or by the D&Os personally, acting as prudent un-insureds. Summary judgment should be denied and Travelers' Rule 12(c) Motion should be granted.

Moreover, because the Defendants do not assert that defense expenses and/or liabilities will reach $40 million in the near future, Defendants' motion for partial summary judgment is not ripe and should be denied on that basis as well.

STATEMENT OF FACTS

As demonstrated by the graphic coverage chart in the Federal Opposition, the Travelers Policy is excess to the primary and six other excess layers of insurance – the Chartis primary, two excess policies issued by Federal, and the four policies issued by the insolvent carriers, The

Home and Reliance.[2] The plain language of the Travelers Policy provides that the Policy is triggered only when (1) Defendants' defense costs and/or liability reaches $40 million; **AND** (2) the underlying insurance have been exhausted "solely as the result of actual payment of losses." As noted in Travelers' Rule 12(c) Motion, the Travelers Policy provides:

> I. INSURING AGREEMENT
>
> ***Coverage hereunder shall attach only after all such Underlying Insurance has been exhausted*** and shall then apply in conformance with the terms conditions and limitations of the Policy immediately underlying this Policy except as specifically set forth in the terms condition and limitations of this Policy.
>
> * * *
>
> IV. DEPLETION OF UNDERLYING LIMIT(S)
>
> ***In the event of the depletion of the limit(s) of liability of the Underlying Insurance solely as the result of actual payment of losses thereunder by the applicable Insurers***, this Policy shall, subject to the limit of liability of the Underwriter and to the other terms of this Policy, continue to apply to losses as excess insurance over the amount of insurance remaining under such Underlying Insurance. In the event of the exhaustion of all of the limit(s) of liability of such Underlying Insurance ***solely as a result of payment of losses thereunder***, the remaining limits available under this Policy shall, subject to the limit of liability of the Underwriter and to the other terms, conditions and limitations of this Policy, continue for subsequent losses as primary insurance and any retention specified in the Primary Policy shall be imposed under this Policy as to each claim made; otherwise no retention shall be imposed under this Policy.

(Sandnes Decl.[3] Ex. 1 at I and IV (emphasis added).)

---

[2] As explained in the Federal Opposition, in these circumstances, the Travelers Policy is also arguably excess to the $1 million dollar Chartis excess policy.

[3] "Sandnes Decl." refers to the December 15, 2010 Declaration of James Sandnes, submitted in support of Travelers' Rule 12(c) Motion [ECF No. 42].

Neither of the two condition precedents to coverage articulated above has been fulfilled. First, as explained in the Federal Opposition, the amount in defense fees and/or liability incurred to date and projected through trial is far below $40 million. Moreover, the total amount of defense fees and/or liability incurred by the D&Os remains highly speculative and uncertain to ultimately reach the $40 million attachment point of the Travelers Policy. Second, the limits of liability of the underlying insurance have not been exhausted by actual payment by anyone.

ARGUMENT

I. The Defendants' Motion is Not Ripe

The issue of whether the Travelers and Federal excess policies provide coverage for a potential Loss for a hypothetical amount is not ripe for adjudication. This issue is even less ripe as to Travelers than it is as to Federal, because the Travelers Policy is far more excess than the Federal Policies. As detailed in the Federal Opposition, all of the defense expenses and settlement payments made under the insurance tower have totaled only approximately $14 million to date, including the Bahamian Litigation and a number of other litigations dating back to the mid-1990's. Most, if not all, of that amount has been paid by the Chartis primary policy and the first Federal policy. The D&Os cannot and have not asserted that the remaining Defense Cost for the Bahamian Litigation will come close to reaching $40 million. (*See* Federal's Local Rule 56.1 Statement ¶ 5.) Thus, regardless of whether the Federal Policies could be implicated by the payment of defense expenses, there simply is no way that defense expenses will reach the Travelers' attachment point.[4]

[4] In this regard, Travelers notes that Section III of the Federal Opposition regarding the duty to defend and Chartis' coverage obligation to drop down and advance defense expenses is not relevant to Travelers.

With respect to settlement, the D&Os have not asked the carriers to consent to any settlement and, indeed, the parties to the Bahamian Litigation have not even discussed the possibility of settlement. (*See id.* ¶ 6.) At bottom, there is far from a "practical likelihood," on this record, that the D&Os will incur a liability that will reach Travelers' $40 million attachment point. *See E.R. Squibb & Sons, Inc. v. Lloyd's & Co.*, 241 F.3d 154, 177 (2d Cir. 2001) (explaining that a matter is ripe only if there is "practical likelihood" that contingencies engaging the insurance coverage will occur). Accordingly, Defendants' motion is not ripe at least as to Travelers.

II. The Travelers Policy has not Been Triggered Because the Plain Language of the Policy and Pennsylvania Law Require that the Underlying Insurance Be Exhausted by Actual Payment of Claims

As just quoted above, the plain language of the Travelers Policy requires exhaustion of underlying insurance by payment of loss. As explained in the Federal Opposition, Pennsylvania law, which applies to this dispute, holds that exhaustion of underlying coverage is "a condition precedent to the excess insurer's liability." *General Refractories Co. v. Allstate Ins. Co.*, 1994 WL 246375, at *4 (E.D. Pa. June 8, 1994). The exhaustion requirement of the policy remains intact even where the policy is silent as to coverage in the event of an underlying insurer's insolvency. (*See* Federal Opposition at 13-22 and cases cited therein).[5]

---

[5] Although the D&Os initially sought, in the alternative, a holding that the excess policies drop down into the coverage attachment points of The Home and Reliance policies, the D&Os have apparently abandoned that argument. This change is understandable given that the D&O cite *M.A.G. Enterprises, Inc. v. National Union Fire Ins. Co.*, No. 3855, 2005 WL 503053 (Pa. Comm. Pl. Feb. 16, 2005) in support of its Motion for Partial Summary Judgment (Def. Mem. at 20), a case that clearly establishes that the excess policies are not required to drop down in the

Pursuant to the Policy provisions quoted above, the Travelers Policy not only requires the "actual payment of losses" but also that the payment be made pursuant to the underlying polices and that it be paid by the insurance companies issuing those policies. (Sandnes Decl. Ex. 1 ("payment of losses thereunder ***by the applicable Insurers***")). While Travelers recognizes that it may be difficult to accept a result in which the insured is denied coverage under its excess policies because of the insolvency of an underlying carrier, the law of Pennsylvania simply does not support an alternate outcome. This result is not intended to create a windfall for the insurer, but rather to honor the terms of the insurance contract, which was bargained and negotiated among sophisticated parties.

As discussed in the 12(c) motion, the existence of underlying performing coverage to adjust the claim within its limits is a bargained for condition of the policy. As noted by Federal, the case on which Defendants heavily rely, *Zeig v. Massachusetts Bonding & Ins. Co.*, 23 F.2d 665 (2d Cir. 1928) supports the enforcement of the exhaustion requirements of the Travelers Policy. There, the Second Circuit explained that parties to an insurance contract could – as the parties to the Travelers Policy did –require exhaustion by payment of claims as a "condition precedent to liability upon the policy, if they chose to do so." *Id.* at 666. *Zeig* was merely interpreting the language of that particular policy under New York, not Pennsylvania law. And, notably, even under *Zeig*, the court made clear that the policy only was required to respond to the extent that the loss exceeded the attachment point.

However, the Court need not directly reach that issue, because even were the Court to

---

circumstance presented here. *Id.* at *5 (explaining that "in Pennsylvania, an excess insurer is not required to drop down to provide primary coverage where the underlying primary insurer is insolvent, unless required to do so by the policy itself").

conclude that it is inappropriate to foreclose excess coverage as a result of the insolvency of the underlying carriers, the result advocated by the D&Os motion certainly finds no support in the law and is plainly inequitable. There is no way to conclude that coverage is triggered when defense costs and/or liability reach the excess carrier's attachment point notwithstanding that neither the underlying insurer nor policyholder actually paid the underlying coverage limits. The most the D&Os could argue for is a ruling that ***if they, in fact, provide in-fill*** for the insolvent carriers, by actually paying out of pocket the amounts that would otherwise have been covered loss paid by the insolvent carriers, then the exhaustion obligations of the Travelers Policy would be met. But that is not what they seek in their motion, so their motion must be denied without the Court needing to reach the hypothetical question of whether, were there such in-fill, the Travelers policy would then be triggered.

CONCLUSION

For all of the reasons set forth above and in the Federal Opposition, the Court should deny Defendants' Motion for Partial Summary Judgment seeking a declaration that the Travelers Policy is triggered once Defendants' defense costs and/or liability reaches $40 million regardless as to whether the underlying policies have been exhausted by payment of claims. Instead the 12(c) motion should be granted.

Dated: New York, New York
January 26, 2010

BOUNDAS, SKARZINSKI, WALSH & BLACK LLC

Of counsel:

Tammy Yuen

By: /s James Sandnes
James Sandnes (JS-8944)

One Battery Park Plaza
New York, New York 10004
(212) 820-7700
jsandnes@bswb.com

Attorneys for Third-Party Defendant Travelers Casualty and Surety Company

4845-7622-6824, v. 1